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ABSTRACT

An evaluation was done of the State University of New York (SUNY) Research Foundation's controls over direct expenditures for research and sponsored activities. The Foundation is a private, non-profit educational corporation established to expand the educational mission of SUNY through fund raising, administration of gifts and grants, and promotion and administration of externally-sponsored research. From June 30, 1987 to June 30, 1992 the Foundation has seen a large increase in expenditures from $189 million to $289 million. The audit covered practices related to controls over direct expenditures for research and sponsored activities. It examined more than 50 personal service expenditures and almost 100 other-than-personal-service expenditures from 17 sponsored projects at two campuses (Buffalo and Stony Brook). The audit found that, except for controls over certain subcontractor costs, the internal control structure appears to be adequate to ensure that expenditures are appropriate. About 10 percent of direct expenditures are payments to subcontractors. These have increased from $7.7 million in 1987 to $22.4 million in 1992. Examination of selected vendors found that Foundation payments were based on summary billings with no supporting documentation. Other irregularities included inappropriately charged consultant fees, unsupported expenses, and over-billings. Includes the comments of Foundation officials. (JB)

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ED 369 359

# New York
# Office of the State Comptroller
# Division of Management Audit

STATE UNIVERSITY OF NEW YORK
RESEARCH FOUNDATION
CONTRACT AND OVERHEAD COSTS

HE027 398

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# State of New York
# Office of the State Comptroller

**Division of Management Audit**

**Report 93-S-64**

The Honorable D. Bruce Johnstone
Chancellor
State University of New York
State University Plaza
Albany, New York 12246

Dear Chancellor Johnstone:

The following is our report on the State University of New York Research Foundation's controls over selected expenditures.

This audit was performed pursuant to the State Comptroller's authority as set forth in Section 1, Article V of the State Constitution and Section 8, Article 2 of the State Finance Law.

This report was prepared under the direction of John T. Walsh, Audit Director. Other major contributors are listed in Appendix A.

*Office of the State Comptroller*
*Division of Management Audit*

December 31, 1993

# Executive Summary

# State University of New York Research Foundation Controls Over Direct Costs

## Scope of Audit

The Research Foundation of the State University of New York (Research Foundation or Foundation) was chartered in 1951 by the Board of Regents as a private, non-profit educational corporation. The purpose of the Research Foundation is to expand the educational mission of the State University through fund raising, to administer gifts and grants, and to promote and administer externally-sponsored research. The Research Foundation operates branches at each of the University System's State-operated campuses, with a corporate headquarters in Albany (Central Office).

During the two fiscal years ended June 30, 1992, the Research Foundation spent almost $597 million on research and sponsored activities. The Research Foundation has seen a dramatic increase in expenditures during the past six years. In the fiscal year ended June 30, 1987, expenditures exceeded $189 million, while in the 1992 fiscal year, they increased to $298 million at 29 SUNY campuses and Central Administration.

We audited Research Foundation practices related to controls over direct expenditures for research and sponsored activities. We examined more than 50 personal service and almost 100 other-than-personal-service expenditures from 17 sponsored projects at the two campuses we visited (University Centers at Buffalo and Stony Brook). Our audit did not include a review of the Research Foundation's practices related to indirect expenditures. Our Staff Study of the States' Research Foundations (93-D-4 issued in July 1992) addressed indirect costs.

Our audit addressed the following question about the Foundation's operations:

- Does the Research Foundation have adequate controls to ensure that direct expenditures for research and sponsored activity are appropriate?

## Audit Observations and Conclusions

Except for controls over certain subcontractor costs, we conclude that the internal control structure in place appears adequate to ensure that research and sponsored-activity expenditures are appropriate. (See p. 5)

The Research Foundation sometimes uses subcontractors to perform or complete a designated portion of research or sponsored activity. About 10 percent of the Foundation's direct expenditures are payments to subcontractors. Payments to subcontractors increased from $7.7 million in 1987 to $22.4 million in 1992. During fiscal years 1990-91 and 1991-92, the Research Foundation paid subcontractors more than $46 million. Almost 89 percent, approximately $41 million, of payments were made by five Research Foundation locations (University Centers at Albany, Buffalo, and Stony Brook; the Health Science Center at Brooklyn; and the Research Foundation Central Office).

For these locations, we obtained a detailed list of subcontractor payments, arranged by subcontractor and by location. We identified subcontractors who received payments in excess of $90,000 in either fiscal year of our audit period. We then judgmentally selected six vendors from this list for site visits and audit testing. We found that the Research Foundation's payments to subcontractors are based on summary billings with no supporting documentation. These billings provide little, if any, assurance that the charges to the subcontract were actually incurred and were reasonable and appropriate expenditures.

The results of our site visits indicate that, although 100 percent of the subcontract costs submitted by some vendors are adequately supported, reasonable and appropriate, some costs submitted by other vendors are not. For example, one contractor inappropriately charged $8,731 for consultant fees and fringe benefit costs to its subcontract with the Research Foundation. Another contractor also billed for more than $274,000 in salaries and $889 in other expenses that were not sufficiently supported. In total, we identified more than $38,000 of potential over-billings and approximately $311,000 of expenses that were not sufficiently supported. In addition, we identified a $67,751 advance to a subcontractor that was not repaid. The details of our site visits are summarized in this report by subcontractor. (See pp. 8-12)

## Comments of Research Foundation Officials

A draft copy of this report was provided to Research Foundation officials for their review and comment. Their comments, as appropriate, are shown in the related sections of this report. The full test of the Research Foundation's response is included as Appendix B.

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# Introduction

## Background

The Research Foundation of the State University of New York (Research Foundation or Foundation) was chartered in 1951 by the Board of Regents as a private, non-profit educational corporation. The purpose of the Research Foundation is to expand the educational mission of the State University through fund raising, to administer gifts and grants, and to promote and administer externally-sponsored research.

It is governed by a 15-member board of directors, including the Chancellor of the State University, who serves as chairman, ex officio. In accordance with the Foundation's charter, the remaining board members are appointed by the State University Board of Trustees. The Foundation Board appoints all Foundation corporate officers, including a President, Executive Vice President and Secretary Treasurer. As a private corporation under contract to the State University system, the Research Foundation acts as the central management and policy agency for system-wide research. State University policy requires that all external support for sponsored program activity be administered by the Foundation.

The Research Foundation is responsible for the fiscal management and administration of all SUNY research and research-related programs. The major functions related to the management of sponsored program funds include the employment of research and other personnel, the purchase of equipment and supplies, and the disbursement of funds for other approved purposes (i.e., rentals, communications, computer services and travel). Administrative functions include controlling and accounting for expenditures, preparing periodic reports, conducting internal audits, providing banking services, and managing cash flow investments.

During the two fiscal years ended June 30, 1992, the Research Foundation spent almost $597 million on research and sponsored activities, representing a dramatic increase in expenditures during the past six years. In the fiscal year ended June 30, 1987, expenditures exceeded $189 million, while in the 1992 fiscal year, they increased to $298 million at 29 SUNY campuses and Central Administration. The four SUNY University Centers (at Albany, Binghamton, Buffalo and Stony Brook) and the two Health Science Centers (at Brooklyn and Syracuse) account for almost 82 percent of the expenditures for

research and sponsored activities. During the fiscal year ended June 30, 1992, these locations spent $244 million.

## Audit Scope, Objectives and Methodology

We audited Research Foundation practices related to controls over direct expenditures for research and sponsored activities for the period April 1, 1990, through March 31, 1993. Our audit did not include a review of the Foundation's practices related to indirect expenditures. Our Staff Study of the States' Research Foundations (93-D-4 issued in July 1992) addressed indirect costs. The primary objective of our audit was to determine whether the Foundation has established adequate controls to ensure that direct expenditures for research and sponsored activity are appropriate. To accomplish this objective, we reviewed applicable policies, procedures, rules and regulations; interviewed Foundation officials at the Central Office and select campuses; examined a sample of expenditure transactions; and made visits to the work sites of a sample of subcontractors to audit the support for their billings to the Foundation.

We conducted our audit in accordance with generally accepted government auditing standards. Such standards require that we plan and perform our audit to adequately assess those operations of the Research Foundation which are included within the audit scope. Further, these standards require that we understand the Foundation's internal control structure and its compliance with those laws, rules and regulations that are relevant to Foundation operations which are included in our audit scope. An audit includes examining, on a test basis, evidence supporting transactions recorded in the accounting and operating records and applying such other auditing procedures as we consider necessary in the circumstances. An audit also includes assessing the estimates, judgments and decisions made by management. We believe that our audit provides a reasonable basis for our findings, conclusions and recommendations.

We use a risk-based approach when selecting activities to be audited. This approach focuses our audit efforts on those operations that have been identified through a preliminary survey as having the greatest possibility for needing improvement. Consequently, by design, finite audit resources are used to identify where and how improvements can be made. Thus, little audit effort is devoted to reviewing operations that may be relatively efficient or effective. As a result, our audit reports are prepared on a "exception basis." This report, therefore, highlights those areas needing improvement and does not address activities that may be functioning properly.

## Response of Research Foundation Officials to Audit

A draft copy of this report was provided to Research Foundation officials for their review and comment. Their comments, as appropriate, are shown in the related sections of this report. The full text of the Research Foundation's response is included as Appendix B.

# Evaluation of Internal Control Structure

The Research Foundation operates branches at each of the University System's State-operated campuses, with a corporate headquarters in Albany (Central Office). Campus responsibility and authority to conduct certain administrative operations of the Foundation are clearly defined with the Central Office controlling the financial operations of the Foundation. Operating systems, policies and procedures are designed by Foundation management and communicated to the operating units through manuals and other communiques. Operations are examined periodically by the Foundation's Internal Audit group, and an external audit is performed annually.

We examined more than 50 personal service and almost 100 other-than-personal-service expenditures from 17 sponsored projects at the two campuses we visited (University Centers at Buffalo and Stony Brook). Except as noted in the section of this report titled "Oversight of Subcontractor Costs," we conclude that the internal control structure in place appears adequate to ensure that research and sponsored-activity expenditures are appropriate. During our testing of transactions, we found some instances of noncompliance with Research Foundation procedures. Such exceptions were discussed with Foundation officials.

# Oversight of Subcontractor Costs

The Research Foundation sometimes uses subcontractors to perform or complete a designated portion of research or sponsored activity. About 10 percent of the Foundation's direct expenditures are payments to subcontractors. This category of expense has exhibited a tremendous growth over the past few years, showing an increase of approximately 190 percent since 1987. Payments to subcontractors increased from $7.7 million in 1987 to $22.4 million in 1992.

Normally, it is not possible for the persons who authorize payments to subcontractors to witness how the funds are spent. Therefore, the Research Foundation should institute adequate controls to ensure that subcontract expenditures are appropriate and adequately supported, and that subcontractors comply with applicable sponsor guidelines and Foundation policies and procedures. Considering the substantial amount of funds expended on subcontracts each year, the Foundation should ensure that the expenses billed were actually incurred and were appropriate charges to the subcontract.

We found that the Research Foundation's payments to subcontractors are based on summary billings with no supporting documentation. These billings provide little, if any, assurance that the charges to the subcontract were actually incurred and were reasonable and appropriate expenditures.

During fiscal years 1990-91 and 1991-92, the Research Foundation paid subcontractors $46 million. Almost 89 percent, approximately $41 million, of payments were made by five Foundation locations (University Centers at Albany, Buffalo, and Stony Brook; the Health Science Center at Brooklyn; and the Research Foundation Central Office). For these locations, we obtained a detailed list of subcontractor payments, arranged by subcontractor and by location. We identified subcontractors who received payments in excess of $90,000 in either fiscal year of our audit period. We then judgmentally selected six vendors from this list for site visits and audit testing. In total, the six vendors we selected received approximately $2 million in subcontract payments from the Research Foundation during the two fiscal years covered by our audit. These payments represented about 4 percent of the Foundation's total subcontract costs for the period.

The results of our site visits indicate that, although 100 percent of the subcontract costs submitted by some vendors are adequately supported, reasonable and appropriate, some costs submitted by

other vendors are not. For example, one contractor inappropriately charged $8,731 for consultant fees and fringe benefit costs to its subcontract with the Research Foundation. Another contractor also billed for more than $274,000 in salaries and $889 in other expenses that were not sufficiently supported. In total, we identified more than $38,000 of potential over-billings and approximately $311,000 of expenses that were not sufficiently supported. In addition, we identified a $67,751 advance to a subcontractor that was not repaid. The details of our site visits are summarized in this report by subcontractor.

Research Foundation officials indicated that they are in the process of investigating the potential over billings and that they have recovered the outstanding advance noted in this report.

## Subcontractor A

A not-for-profit community organization entered into a subcontract with the Research Foundation at the University Center at Albany to participate in a program entitled "State Legalization Impact Assistance Grant (SLIAG)," to provide instruction that would enable Eligible Legalized Aliens (ELAs) to meet the minimum educational requirements for permanent residence. The subcontract permits the subcontractor to charge for allowable costs incurred or a set amount based upon criteria up to the maximum amount of the subcontract.

For the 1990-91 and 1991-92 fiscal years, the Foundation paid the subcontractor $314,365. When we tested $127,969 (40.7 percent) of the payments to the subcontractor, we found that the appropriateness of certain charges was questionable, some costs had not actually been incurred, other costs were not sufficiently supported, and some costs had been charged before they were incurred.

We found that the subcontractor charged $29,084 for computer equipment that was used to benefit the SLIAG program only during the final four months of the subcontract. The computer equipment was budgeted for the subcontract period of October 1, 1990, through September 30, 1991, during which time the subcontractor was to offer computer literacy courses according to the subcontract agreement. The subcontractor ordered the computer equipment on August 1, 1991, ten months into the subcontract period; and received it on September 13 through 16, 1991, just before the end of the agreement period. Computer literacy courses were not offered by the subcontractor in that subcontract period; nor were such courses offered in the first five months of the next and final subcontract period, October 1, 1991, through June 30, 1992. The subcontractor did not use the equipment for computer literacy courses until March 1992. While the expense was budgeted for, we question whether the cost of the equipment was a reasonable and appropriate charge to

the subcontract, considering the limited amount of time the equipment was actually used to benefit the program.

We also found that the subcontractor had charged the Research Foundation $125 for the purchase of a pager, which included an activation fee and a three-month service charge. The subcontractor made this purchase on June 30, 1992, the last day of the SLIAG program. We believe this is not a reasonable or appropriate charge to the subcontract. The timing of the purchase clearly shows that the pager was not utilized for the benefit of the SLIAG program.

The subcontractor charged the Research Foundation $20,000 for administrative salaries for the period October 1, 1991, through June 30, 1992, and $16,500 for outreach services for the period October 1, 1990, through June 30, 1992. We found that the subcontractor did not maintain sufficient documentation to support the charges to the subcontract. The U.S. Office of Management and Budget (OMB) Circular A-122, which sets forth guidelines for Federally funded subcontracts, states that the distribution of salaries and wages must be supported by personal activity reports. During the period for which the costs were charged to Albany, payments to the subcontractor's Executive Director for administrative services were not supported by personal activity reports. Also, personal activity reports for employees providing outreach services did not indicate when they provided these services or how much of their time was attributed to outreach.

We found that the subcontractor had overstated by $528 the instructional salary costs billed to the Research Foundation in March 1991. The subcontractor also overstated the employee benefits cost by $40 for the applicable FICA. During the subcontract period of October 1, 1990, through September 30, 1991, the subcontractor prebilled the Foundation for the cost of equipment items and outreach services. These costs were not actually incurred until after the Research Foundation had paid the subcontractor.

## Subcontractor B

A subcontractor with the Research Foundation at the University Center at Buffalo agreed to provide "after school programs designed to complement the public school curriculum and to increase levels of performance, and interest, in higher education and career oriented employment." The charges to this subcontract were for salaries and benefits of the subcontractor's employees, who ran the programs. During the fiscal years of 1990-91 and 1991-92, the subcontractor received more than $221,000 in subcontract payments. When we tested $27,832 (12.6 percent) of these payments, we found that the appropriateness of several salary charges was questionable; and that

the fringe benefit charge had been applied erroneously in some cases.

We found that the subcontractor had paid $17,477.50 to some employees but had not incurred any fringe benefit costs related to those payments. Although no fringe benefit costs had been incurred, the subcontractor erroneously included these costs in the amounts billed the Research Foundation. We found that $5,116 had been paid by the subcontractor for consultant services. The subcontractor erroneously billed the Research Foundation for fringe benefit costs on these expenses. In total, the subcontractor over-billed for $3,615 in fringe benefit costs that had not been incurred. Furthermore, although the consultants did perform services that were beneficial to the program, the subcontract indicates that payments should be made for employees of the subcontractor and does not provide for consultant costs. Therefore, the payments to these consultants is a questionable charge to the subcontract.

## Subcontractor C

A subcontractor entered into a subcontract with the Research Foundation at the University Center at Buffalo to provide a dental program with three objectives; 1) to train dental Fellows in the provision of services to severely disabled individuals, 2) to provide dental services to severely disabled individuals at a number of sites throughout the community and to provide all of the dental services for a Developmental Disability Service Office, and 3) to facilitate the availability of proper dental care for severely disabled individuals in the community. The charges to the subcontract included, among others, salaries for individuals involved in the program, stipends to dental students, and reimbursement for educational expenses. During the 1990-92 fiscal years, the subcontractor received more than $315,000 in subcontract payments. We tested 100 percent of the payments made by the Foundation to the subcontractor. We found that the charges to the subcontract appeared reasonable, but the documentation to support salary and educational expense charges was not adequate.

The subcontract requires the "contractor to maintain appropriate and complete accounts, records, documents, and other evidence showing and supporting all costs incurred" under the subcontract. We found that in general the subcontractor did not maintain appropriate and complete records. For example, the largest category of expense charged to this subcontract for the period we reviewed was salaries, which totaled more than $274,000 or about 87 percent of total charges. We found that the individual in charge of the program under the subcontract did not require employees to submit any sort of time-reporting documents. Moreover, personnel files were not maintained for these individuals.

Other charges to this subcontract included $1,295 in educational expenses. The support for $889 of these expenses was weak, often consisting of cancelled checks with no corresponding invoices or receipts. The subcontractor's record-keeping procedures did not produce "appropriate and complete" documentation to support the charges to the Research Foundation, as required by the subcontract language.

## Subcontractor D

A subcontractor entered into a subcontract with the Research Foundation at the University Center at Stony Brook to participate as a clinical trial subunit studying intravenous drug user and minority populations in Stony Brook's AIDS Clinical Trials Group (ACTG) project. The charges to the subcontract included salaries and FICA for employees working on the project; and reimbursement for patient expenses, equipment, books and journals, travel, office supplies, other direct expenses and indirect costs. During the 1990-92 fiscal years, the subcontractor was paid $348,590 by the Research Foundation. This included a $67,751 advance payment, and reimbursements of $66,256 for indirect costs and $214,583 for direct expenses. We tested $209,262 (98 percent) of the direct expenses billed to the Foundation by the subcontractor. We found that all of the subcontract charges included in our testing had been supported adequately, and were reasonable and appropriate charges to the subcontract.

The Research Foundation's subcontract agreement with the subcontractor for the period September 30, 1990, through August 31, 1991, provided for Stony Brook to make an advance payment to the subcontractor of 25 percent ($67,751) of total compensation ($271,003), and recover the advance by holding it against and deducting it from the fourth quarterly invoice. The Foundation has procedures to ensure that subcontract terms and conditions are complied with before payments are made. The Foundation paid the advance to the subcontractor on March 29, 1991, but overlooked the subcontract provision to recover the funds against the fourth quarterly invoice. The advance should have been recouped by the Foundation on October 23, 1991, when the forth quarterly payment was made . The subcontractor was overpaid $67,751, and to date the overpayment has not been recovered. The Foundation should recover this overpayment from the subcontractor, and should ensure in the future that each research location complies with the terms and conditions of subcontracts by reinforcing implementation of its policies and procedures.

## Subcontractors E and F

An energy and environmental consulting company entered into a subcontract with the Research Foundation at the University Center at Albany for a research project to study the atmospheric effects on forests. The subcontractor's responsibilities during the study were administrative, including data management, quality assurance and technical coordination functions for the study. Several other subcontractors directly performed the research activities. All payments were made through the administering subcontractor to the other subcontractors. We found that the charges included in our testing had been adequately supported.

A company subcontracted with the Research Foundation at the University Center at Buffalo to provide Comprehensive Genetic Services for a specified "catchment area." The charges to the subcontract included, among other expenses, salaries and corresponding benefits for employees providing the services, and reimbursement for office supplies. During the 1990-92 fiscal years, the subcontractor received more than $345,000 in subcontractor payments. We tested $209,807 (61 percent) of the payments made to the subcontractor. We found that all of the subcontract charges included in our testing had been supported adequately, and were reasonable and appropriate charges to the subcontract with the Foundation.

### Recommendations:

1. Investigate potential over-billings identified in this report. Recover over-billed amounts, where appropriate.

2. Conduct periodic audits of subcontractors.

3. Recover the $67,751 advance payment from the subcontractor and ensure that regional locations comply with policies and procedures related to advance payments.

Foundation officials agree with the recommendations and have indicated how the recommendations have already or will be implemented.

# Major Contributors to This Report

Marvin Loewy, Audit Manager
Martin Chauvin, Audit Supervisor
William J. Furman, Auditor-in-Charge
Maureen Costello, Lead Auditor
Michael Muth, Staff Auditor
Marticia Madory, Editor

**The Research Foundation**
of State University of New York

September 10, 1993

OFFICE OF THE STATE COMPTROLLER
ROBERT H. ATTMORE
DEPUTY COMPTROLLER

SEP 1 1993

MGMT. AUDIT &
FINANCIAL REPORTING

Mr. Robert H. Attmore
Deputy Comptroller
Office of the State Comptroller
A.E. Smith State Office Building
Albany, New York 12236

RE: Draft Audit Report 93-S-64

Dear Mr. Attmore:

This letter represents The Research Foundation of State University of New York's formal comments on the findings and recommendations contained in the above draft report in response to your letter of August 17, 1993.

We are pleased that the State Comptroller has concluded that the Foundation's internal control structure "appears adequate to ensure that research and sponsored activity expenditures are appropriate" with the exception noted.

We are in the process of investigating the potential over-billings noted and will take steps to recover any actual over-billings. We have issued a new invoicing process to be utilized for sub-contractors that will reduce the chances of billing errors.

We are appreciative of the assistance rendered to us by the Office of the State Comptroller's auditors in auditing several sub-contracts. That activity augmented the on-going activity of our Internal Audit Department. We plan to increase our internal audits of sub-contractor activity.

The advance payment noted in the report to a sub-contractor has been recovered. We are reminding our operating locations across the State of the importance of complying with our advance payment policies and procedures in place.

Finally, we question the applicability of Section 170 of the Executive Law to The Research Foundation of State

**Appendix B**

Executive Vice President, State University of New York, Albany, New York 12246 (518) [illegible]

University of New York. It is the opinion of our Counsel that the law is not applicable since we are a private corporation functioning under a formal contract with the University.

Sincerely,

John F. Buckhoff, Jr.

c: Chairman Johnstone
President Burke
Mr. Fletcher
Mr. Wolfe